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SIPDIS

STATE FOR DRL/ILCSR AND EUR/AGS; LABOR FOR ILAB
(BRUMFIELD); TREASURY FOR OASIA
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MATTHEWS

SENSITIVE BUT UNCLASSIFIED

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TAGS: [ELAB](#) [ECON](#) [EFIN](#) [PREL](#) [PGOV](#) [GM](#)
SUBJECT: THE WRONG SIGNAL AT THE WRONG TIME:
- SPD DEBATES ECONOMIC REFORM

REF: BERLIN 1977 (SPD Conference)

¶1. (SBU) Summary. No tectonic shift in German economic policy came out of the SPD convention, perhaps, but the SPD's labor reforms could mark the beginning of a rollback in Schroeder's "Agenda 2010" reforms, a source at the Labor Ministry told the Embassy. The resolution to block privatization in particular sent an undesirable message to investors. Together with the CDU/CSU, the market-oriented SPD faction within the government would resist measures that raised the deficit, and could probably block any drastic efforts to augment the welfare state, but in this environment, further structural economic reform in the Grand Coalition government seemed unlikely. End Summary.

¶2. (U) On October 30, EMIN and Labor Specialist met Dr. Guenther Horzetzky, Director General of the Policy Planning Division in the Ministry of Labor and Social Affairs in Berlin. Close to Labor Minister Muentefering, the dyed-in-the-wool Social Democrat and long-term union officer is the "brains" behind many policy initiatives of the Ministry and remains wedded to Schroeder's market-oriented reforms, notably in the area of labor liberalization. He served in the Chancellery from November 2002 to November 2005 and was of one of many co-authors of Schroeder's Agenda 2010.

SPD Party Convention

¶3. (SBU) The resolutions at the SPD's recent convention calling for a partial rollback of former Chancellor Schroeder's reforms did not reflect the agenda of the party leadership so much as a spontaneous shift by the rank and file back toward the SPD's traditional social democratic roots, Horzetzky said. He was uncertain whether the proposal to expand benefits for older unemployed workers presaged other steps to roll back Schroeder's progressive programs. In general, however, the party convention -- by inter alia adopting resolutions to kill

privatization of the German railway (Deutsche Bahn), introduce a uniform national minimum wage, and regulate temporary work had sent a "disastrous signal to capital markets," in Horzetzky's view.

No Stopping Extension of Some Benefits

14. (U) At first glimpse the positions of the coalition partners regarding the extension of benefits for older workers seemed to be not far apart. Both parties favored extension of unemployment benefits for over-50 workers - no heavy lifting required here, with 80 percent public support for such a move. Horzetzky said that the SPD leaders will remind Chancellor Merkel of a similar resolution adopted at the CDU convention in November last year (which ironically, the SPD had then opposed on the grounds that it was a reversal of Agenda 2010). When it came to details, however, there were fundamental differences, particularly over how to finance the extended benefits. The CDU was strictly opposed to any solution that would require additional funding from the federal budget, whereas the SPD wanted to dip into the current surplus of the federal unemployment insurance fund (BA).

15. (U) Beneath the surface, there was intense debate within the SPD itself over where the money would come from. Officially, the SPD argued that the 6.5 billion euros (\$9.1 billion) surplus

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could easily take care of the hand-outs, which it variously estimated at 800 million to 1.1 billion euros annually. However, on October 30 the BA warned that this estimate was way too optimistic. It projected that the new benefits could cost up to 2.9 billion euros (\$4.6 billion) annually. Costs could climb even higher were the economy to slow down, and joblessness rise. Privately, Finance Minister Steinbrueck (SPD), a budget hawk, was reportedly displeased at the SPD's direction, yet was forced into silence.

16. (SBU) It could be worse if other SPD resolutions were to come into law. "By raising the retirement age to 67 and limiting the duration of benefits, we (read: Schroeder's Red-Green government) tried to stop the practice of early retirement," Horzetzky said. He admitted that Agenda 2010 was widely perceived as unfair to people who had paid their unemployment and social security premiums for decades, but demographic realities required a pullback. "We did not explain our intentions well enough" to the public, he lamented.

Next Steps

17. (SBU) Horzetzky expected tough negotiations between the coalition parties at forthcoming meetings of the steering committee, where the CDU/CSU had announced it would block several of the SPD proposals. He predicted Labor Minister Muentefering and Finance Minister Steinbrueck, with strong CDU/CSU support, would be able to delay any solution that was not "cost neutral" - a formulation that was subject to multiple interpretations. The SPD's call for a national minimum wage of 7.5 euros (nearly \$11) an hour would go nowhere given stiff opposition from the

CDU/CSU, which argued that it would lead to job losses. The coalition might agree on the lowest possible denominator, he said: Merkel would "grudgingly" agree to extend the minimum wage to postal workers.

Privatization of Deutsche Bahn

18. (U) In Horzetzky's view, the SPD's opposition spelled doom to privatization of Deutsche Bahn. If the SPD's insisted on reserving 51% of the shares for the government, 25% as "Peoples' Shares" without voting rights, and only 24% (with voting rights) for private interests, he said, strategic investors would be scared away. Leading CDU politicians have already indicated they would want to postpone a decision on privatization of Deutsche Bahn until after the next federal elections in 2009.

"Mrs. Feel Good" in a Wait-and-See Mode

19. (SBU) Horzetzky rejected allegations, especially in the Western press, that Chancellor Merkel (whom he jokingly called "Mrs. Feel Good") had lost her taste for reform, or that she had shied away from making hard decisions. He said she was in a very comfortable position, as the SPD convention had actually played into her hands, giving her several options. She could stay with the SPD for the rest of the legislative term, or she could try to force early elections (given her high ratings in the polls). Nonetheless, nothing in Horzetzky's prognosis indicated we could expect bold new domestic economic initiatives until after the next elections.

TIMKEN JR